No. 85-1736

In The
# Supreme Court of the United States
October Term 1985

JERSEY SHORE STATE BANK,
*Petitioner,*

v.

UNITED STATES OF AMERICA,
*Respondent.*

**ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT**

## BRIEF OF AMICUS CURIAE FIRST ALABAMA BANK IN SUPPORT OF PETITIONER

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## QUESTIONS PRESENTED

Section 6303(a) provides that the government, upon choosing to assess taxes unpaid by an employer, must give notice to each person liable for the unpaid tax. The questions presented are: (a) whether, as a prerequisite to the government's maintenance of a civil suit to collect a lender's § 3505 derivative liability for the assessed taxes, the government must comply with the general notice requirement of § 6303(a) by giving notice of the assessment to the lender, and (b) whether in the absence of such notice, the statute of limitation as it applies to the lender is extended.

## TABLE OF CONTENTS





## TABLE OF AUTHORITIES

TABLE OF AUTHORITIES—Continued





TABLE OF AUTHORITIES—Continued

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### INTEREST OF AMICUS CURIAE

Amicus curiae, First Alabama Bank, successor to The Merchants National Bank of Mobile (hereinafter "MNB"), is currently Respondent to a petition for writ of certiorari to the Eleventh Circuit Court of Appeals filed by the United States of America, No. 85-1480. The issue in that pe-

tition is identical to the one presented herein, though additional issues have been raised in a cross-petition for writ of certiorari filed by Respondent therein. This amicus curiae has received written consent from all parties to file this brief. (Appendix, 1a-2a).

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## SUMMARY OF ARGUMENT

The government has argued that this Court should interpret the clear and unambiguous language of § 6303(a) so as to cause it to fit neatly within its administrative practice of tax collection. Its appeal is addressed to the wrong forum, however, for it should seek relief from Congress and not this Court if it wishes to modify the simple yet meaningful § 6303(a) procedural safeguard for lenders subject to § 3505 liability.

The Third Circuit Court of Appeals in *United States v. Jersey Shore State Bank,* 781 F.2d 974 (3rd Cir. 1986) (Weis, J. dissenting) was the first appellate court to hold that the Congressionally mandated § 6303(a)[1] notice of the assessment of unpaid taxes is not required to be given a lender before maintenance of a suit to collect purported lender's derivative liability for those taxes under § 3505. Both the Seventh Circuit in the *United States v. Associates Commercial Corp.,* 721 F.2d 1094 (7th Cir. 1983) and the Eleventh Circuit in *United States v. Merchants National Bank of Mobile,* 772 F.2d 1522 (11th Cir. 1985) (per curiam), petition for *cert.* pending, No. 85-1480, had previously held that such notice is required by the plain words of the statute. They each rejected the government's arguments that § 6303(a) applied only to administrative collection proceedings and that giving § 6303(a) notice to lenders is impossible.

[1]All references are to the Internal Revenue Code of 1954 (26 U.S.C.) unless otherwise noted.



Subsequent to the divided opinion of the Third Circuit in *Jersey Shore,* the Ninth Circuit issued its opinion in *United States v. Hunter Engineers & Constructors, Inc.,* No. 84-2652, (May 21, 1986), adopting the rationale of the Third Circuit in *Jersey Shore,* and holding that the government's failure to give the lender (in that particular case, a non-bank lender) § 6303(a) notice of the assessment of unpaid taxes did not bar the subsequent action to enforce § 3505 liability nor prevent the extension of the statute of limitations under § 6502(a)(1) and Treas. Regs. § 31.3505-1(d)(1), 26 C.F.R. § 31.3505-1(a)(1).

As framed by these four (4) opinions, the issues have become (i) whether the government must give § 6303(a) notice of assessment to a lender alleged to be liable under § 3505, and, if so, (ii) whether the consequences of the failure to do so are (a) an absolute bar of civil liability under § 3505 or (b) waiver of the extension of the statute of limitations for commencement of a § 3505 action if such extension is valid in the first place.

The Seventh and Eleventh Circuits correctly read § 6303(a) as being a general rule applicable to all collection methods instituted by the Secretary of the Treasury, unless a special rule applies. Section 3505 and its regulations contain no exception to that general rule.

The government contends that § 6303(a) is restricted to the administrative collection process and has no application to the judicial collection process. This argument focuses on the idea that assessment relates only to administrative collection from the employer and that § 6303(a) notice of the assessment and demand for payment must be sent only to employers and not to lenders, who are liable only by way of civil proceeding. However, § 6303(a) is contained in Subtitle F of the Internal Revenue Code, and Subtitle F controls *all* of the procedures by which the Secretary of the Treasury may institute collection of taxes, including litigation.

Assessment is not a mere formality that relates only to the administrative collection activities against the employer. It acts to automatically extend the statute of limitation under § 6502(a)(1), which has been engrafted intc Treas. Regs. § 31.3505-1(d)(1) for prosecution of a § 3505 claim. Where the employer receives notice of the assessment and the lender does not, it would be manifestly unfair to extend the statute of limitations against both. No other provision of the tax collection process against persons derivatively liable (*e.g.*, § 6672 responsible officer penalties, § 6901 transferee penalties) produces such a prejudicial circumstance and results in such an inherently unfair recovery process. Certainly, Congress recognized this and plainly intended that the lender should receive the sam procedural safeguard as the taxpayer-employer.

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## ARGUMENT

### I. Congress is the only Appropriate Forum for Revision of § 6303(a).

#### A. The Language of §6303(a) is Unambiguous.

The beginning point of interpreting any statute is the language of the statute itself, as noted in *Consumer Products Safety Commission v. GTE Sylvania, Inc.*, 447 U.S. 102, 100 S.Ct. 2051, 64 L.Ed.2d 766 (1980), wherein this Court stated:

> We begin with the familiar canon of statutory construction that the starting point for interpreting a statute is the language of the statute itself. Absent a clearly expressed legislative intention to the contrary, that language must ordinarily be regarded as conclusive.

447 U.S. at 108.

The Seventh Circuit, Eleventh Circuit and Judge Weis, dissenting from the Third Circuit's opinion in *Jersey Shore*, all recognized that the phrase "each person liable for the unpaid tax" in § 6303(a) is not in the least ambiguous.

Judge Weis, in particular, examined the legislative history of both §§ 6303(a) and 3505, rather than limiting his inquiry only to the legislative history of § 6303(a) and Reorganization Plan No. 26 of 1950, 5 U.S.C.A. App. at 274, 15 F.R. 4935, 64 Stat. 1280, and Reorganization Plan No. 1 of 1952, 26 U.S.C.A. § 7804 (Historical Note), 17 F.R. 2243, 66 Stat. 823, as argued by the government to support its contention that § 6303(a) does not require notice to a § 3505 lender.

It is important to note that § 3505 derivative liability did not exist at the time the Reorganization Plans and § 6303(a) were adopted. Judge Weis' clarity in reviewing all appropriate legislative history and synthesizing the interplay of § 6303(a) and § 3505 is succinctly set forth in his dissenting opinion:

> In this case, I cannot even say with assurance that the addition to the statute that the IRS proposes was inadvertently omitted. Certainly, the legislative history of § 6303 provides no basis for such a belief. Moreover, the legislative history of § 3505 does not suggest that notice should not be provided lenders who may be secondarily liable. "Congressional silence, no matter how 'clanging,' cannot override the words of the statute." *Sedima v. Imrex Co., Inc.*, — U.S. —, 105 S.Ct. 3275, 3285 n.13, 87 L.Ed.2d 346 (1985).

781 F.2d at 984.

The majority in *Jersey Shore* failed to address the fact that at the time of adoption of the 1954 Code, there was no derivative liability that did not provide for separate notice and assessment. When Congress used the phrase "each person liable for the unpaid tax" it must have intended to guarantee notice of assessment to each person liable for the unpaid tax. Neither § 3505 or its legislative history indicates any intent to exempt a lender from such notice. Thus, there is no clearly expressed legislative intention which is contrary to the ordinary meaning of the phrase "each person liable for the unpaid tax."

### B. Congress is the Only Proper Forum for the Government to Seek a Rewrite of § 6303(a).

Whatever merit there may be, if any, in the government's argument regarding the duty or burden of giving



notice, it is a matter for Congress, not this Court. Judge Weis, in his dissent to the majority opinion in *Jersey Shore*, answered this argument best:

> The IRS wishes us to redraft that section so that it requires notice only to those individuals against whom taxes have been assessed. The reasons offered for this revision have some logic and would possibly ease administrative burdens on the government, but the arguments are directed to the wrong forum. *They should be presented to Congress, not the courts.*
>
> In *Iselin v. United States*, 270 U.S. 245, 251 (1926), the Supreme Court said that courts should not revise a statute so that "what was omitted, presumably by inadvertence, may be included within its scope. To supply omissions transcends the judicial function."
>
> The courts' limited role was reemphasized in *TVA v. Hill*, 437 U.S. 153 (1978). Once "Congress has spoken in the plainest of words" and "the meaning of an enactment is discerned . . . the judicial process comes to an end. We do not sit as a committee of review, nor are we vested with the power to veto." Courts may not "pre-empt congressional action by judicially decreeing what accords with 'common sense and the public weal.' Our Constitution vests such responsibilities in the political branches." *Id.* at 194-95.

781 F.2d at 983-84 (emphasis added).

For these reasons, this Court should enforce the plain meaning of the language of § 6303(a), leaving the government to petition Congress for any requested revision.

**II. The Government's Failure to Give Timely §6303(a) Notice of Assessment to a Lender Bars any Suit Alleging Lender's Liability under §3505.**

**A. The Notice was Required to be Given.**

1. **The Genesis of §6303(a).**

Section 6303(a) provides as follows:

> *General Rule* - Where it is not otherwise provided by this title, the secretary or his delegate *shall*, as soon as practicable, and within sixty (60) days, after the making of an assessment of a tax pursuant to section 6203, *give notice to each person liable for the unpaid tax*, stating the amount and demanding payment thereof. Such notice shall be left at the dwelling or usual place of business of such person, or shall be sent by mail to such person's last known address. [Emphasis added].

Section 6303(a) was derived, in part, from § 3655 of the Internal Revenue Code of 1939 (hereinafter "1939 Code"), which provided:

> *Delivery.* Where it is not otherwise provided, the collector shall in person or by deputy, within ten (10) days after receiving any list of taxes from the Commissioner, give notice to each person liable to pay any taxes stated therein, to be left at his dwelling or usual place of business, or to be sent by mail, stating the amount of such taxes and demanding payment thereof.

The "list of taxes from the Commissioner" identified in § 3655 refers to § 3641 of the 1939 Code, which provided that "[t]he Commissioner shall certify a list of such assessments when made to the proper collectors, respectively, who shall proceed to collect and account for the taxes and penalties so certified."



Thus, prior to adoption of the 1954 Code by Congress,[2] only the Tax Collector was required to give notice, and only to each person liable to pay any taxes stated in the certified list of assessments made by the Commissioner. This dichotomy of function between the Tax Collectors, on the one hand, and the Commissioner of Internal Revenue, on the other hand, appears to be the pivotal rationale in those cases which addressed a Tax Collector's failure to give notice of the assessment under the predecessors to § 6303(a). *See Jenkins v. Smith*, 99 F.2d 827 (2d Cir. 1938) (§ 1545 of Internal Revenue Code of 1926); *United States v. Erie Forge Co.*, 191 F.2d 627 (3rd Cir. 1951) (§ 3655 of the 1939 Code).

The Second and Third Circuits held in *Jenkins* and *Erie Forge*, respectively, that only the Tax Collector, who could collect taxes only by administrative collection proceedings, was barred from collection by failure to give notice under the predecessors to § 6303(a), but that such failure was "immaterial in an action by the United States, since such a suit is brought 'either upon the assessment, or upon the duty imposed by the statute alone'." 99 F.2d at 828; 191 F.2d at 631.[3]

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[2]Actually, Reorganization Plans No. 26 of 1950 and No. 1 of 1952 began the reorganization of the Department of Treasury by transferring the functions of the Commissioner and Tax Collectors, among others, to the Secretary and abolishing those functionless offices, respectively. These plans are carried over into the 1954 Code under § 7804(a). For ease of reference, MNB shall refer to adoption of the 1954 Code as the focal point herein.

[3]The rationale for such holdings would appear to be based on the government's right to bring suit against the employer

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In adopting the 1954 Code, particularly § 6303(a),[4] Congress did not address the implication of placing the burden of notice and demand on the Secretary after transfer of the functions of the Tax Collectors and abolishment of those presidentially appointed offices, any inherent changes in procedure caused by combination of the functions of the Commissioner and Tax Collectors under the office of the Secretary, nor the conversion of the notice and demand statute into a "general rule" as opposed to a "delivery" rule under the predecessor statutes.

Moreover, Congress did not address the inclusion of the phrase "after the making of an assessment of a tax pursuant to § 6203" in place of the predecessor phrase "after receiving any list of taxes from the Commissioner" in § 3655 of the 1939 Code. Section 6203[5] specifically recognizes the burden of assessment on the Secretary and

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based simply on its common law right to sue on the debt, which exists independently of any statute, and that the Commissioner, not the Tax Collector, was the only officer authorized to proceed by suit under § 3740 of the 1939 Code and its predecessors, and he had no statutory duty to provide notice to anyone. *See, e.g., Dollar Savings Bank v. United States*, 86 U.S. (19 Wall.) 227, 239-40 (1874); *Damsky v. Zavatt*, 289 F.2d 46, 51 (2nd Cir. 1946). *See also United States v. Jersey Shore State Bank*, 781 F.2d 974, 979 n.4 (3d Cir. 1986).

[4]Congress stated in the Committee Reports that § 6303 "contains two changes from existing law", neither of which has any particular relevance herein. H.R. Rep. No. 1337, 83rd Cong., 2d Sess. at 405 ([1954] 3 U.S. Code Cong. & Ad. News 4017, 4553); S. Rep. No. 1622, 83rd Cong., 2d Sess. at 574 ([1954] 3 U.S. Code Cong. & Ad. News 4621, 5222-5223).

[5]Section 6203 provides that, "[t]he assessment shall be made by recording the liability of the *taxpayer* . . .". [Emphasis added].



uses the restrictive term "taxpayer" as opposed to the broad phrase "each person liable for the unpaid tax", so that only the taxpayer is assessed. Thus, under the 1954 Code, § 6203 requires the Secretary to assess the liability of the taxpayer-employer by recording same, and then requires the same Secretary to give notice under § 6303(a) of said assessment to "each person liable for the unpaid tax," as opposed to only the "taxpayer" so assessed.[6]

Upon adoption of the 1954 Code, the Secretary exercised all functions of tax collection, whether by administrative process or civil proceedings. The general rules regarding collections therefore require the Secretary to give § 6303(a) notice to each person liable for an assessed tax without reference to the collection mechanism employed.

At the time of adoption of § 6303(a), Congress could not have envisioned nor discussed the effect of the later adoption of lender's derivative liability in § 3505, as such was not even contemplated in 1954. After adoption of the 1954 Code and before enactment of § 3505 in 1966, each person liable for the unpaid tax was given § 6303(a) notice by the government since no statutory derivative liability existed during that period which did not provide

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[6]Furthermore, § 6303(a) is found in Subtitle F of the 1954 Code, entitled "Procedure and Administration", Chapter 64, entitled "Collection", Subchapter A, entitled "General Provisions." Subtitle F also includes § 7401, authorizing the commencement of civil actions by the Secretary "for the *collection* or recovery of taxes . . . ". (Emphasis added). Clearly, Congress did not give the government license to choose which parts of Subtitle F it would apply the general rule of § 6303(a) to and which it would not.

for separate notice and assessment (e.g., § 6672 responsible officer penalties and § 6901 transferee liability).

2. **The Genesis of §3505.**

Section 3505 provides, in part, as follows:

> (a) *Direct Payment by Third Parties*—For purposes of sections 3102, 3202, 3402, and 3403, if a lender, surety, or other person, who is not an employer under such sections with respect to an employee or group of employees, pays wages directly to such an employee or group of employees, employed by one or more employers, or to an agent on behalf of such employee or employees, such lender, surety, or other person shall be liable in his own person and estate to the United States in a sum equal to the taxes (together with interest) required to be deducted and withheld from such wages by such employer.
>
> (b) *Personal Liability Where Funds Are Supplied*—If a lender, surety, or other person supplies funds to or for the account of an employer for the specific purpose of paying wages of the employees of such employer, with actual notice or knowledge (within the meaning of section 6323(i)(1)) that such employer does not intend to or will not be able to make timely payment or deposit of the amounts of tax required by this subtitle to be deducted and withheld by such employer from such wages, such lender, surety, or other person shall be liable in his own person and estate to the United States in a sum equal to the taxes (together with interest) which are not paid over to the United States by such employer with respect to such wages.

Section 3505 was enacted as part of the Federal Tax Lien Act of 1966, Pub. L. 89-719, in order to stem the loss



of revenue occasioned by the practice of financing "net" payrolls by lenders, sureties and other such persons.[7]

In imposing the derivative liability of § 3505 on lenders, and, in effect, creating a new tax liability unknown at common law or in previous Internal Revenue Codes, Congress did not address the procedure and administration for collection of this tax liability, except to advise that the Secretary had to proceed by appropriate civil proceeding. Congress specifically did not address any exemption of § 3505 from the general notice requirements of § 6303(a), nor the extension of the statute of limitations for collection of § 3505 liability by assessment of taxes unpaid by the employer pursuant to § 6502(a)(1).

However, the legislative history of § 3505 indicates that Congress was placing the lender in the shoes of the employer as to liability for the unpaid taxes in the specific cases set forth under § 3505, but restricting the Secretary to appropriate civil proceedings as his sole remedy. Congress stated:

> Third persons who pay wages directly to employees ordinarily have full access to payroll information and, therefore, have essentially the same ability to determine the amount of wages due, and control over funds available for payment, *as is usually true in the case of employers. Therefore, no admin-*

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[7]It is well settled that § 3505 does not require or, indeed, permit a separate assessment to be made against the third party lender, *United States v. First National Bank of Circle*, 652 F.2d 882 (9th Cir. 1981); *United States v. Dixieline Financial, Inc.*, 594 F.2d 1311 (9th Cir. 1979), such that the government must proceed to collect § 3505 liability only by appropriate civil proceedings. *See* H.R. Rep. No. 1884, 89th Cong., 2d Sess. at 65-66 (1966-2 C. B. 815 at 861-62).

*istrative problems are expected in these cases by holding the third parties liable for withholding taxes.* [Emphasis added].

• • •

*Third parties who specifically finance payrolls, although not paying employees directly also are often in positions similar to that of employers.* This appears to be true in those cases where they have actual such knowledge that the employers do not intend to, or are unable to, pay the amount of withholding taxes due the Government. Therefore, in these cases also it would appear practical for those third parties to account for withholding taxes to the Government. [Emphasis added].

H.R. Rep. No. 1884, *supra*, at 20 (1966-2 C. B. at 829); S. Rep. No. 1708, 89th Cong., 2d Sess. at 22 (1966-2 C. B. at 891).

Clearly, Congress set forth the concept of lender's derivative tax liability under § 3505 by placing the lender in the shoes of the employer as to liability for unpaid withholding taxes under those two factual situations. Yet, prior to adoption of § 3505 in 1966, each person liable for those taxes was required to receive notice and demand for payment under § 6303(a) once unpaid taxes had been assessed, and it is abundantly clear that § 3505 does not exclude lenders from the general rules of procedure under Subtitle F.

Must not, then, Congress have intended that the lender, whose liability is derivative of the liability of the employer for failure to pay withholding taxes, receive the same procedural safeguard given the employer, specifically that of § 6303(a) notice? Certainly, Congress knew that § 3505 liability would be subject to the general collection rules, and that § 6303(a), a general collection rule, requires that notice be given not only to the taxpayer, but to "each person liable for the unpaid tax."



Congress does not act in a vacuum and it must be credited with having certain equities and procedural safeguards in mind when enacting § 3505. In order to extend the statute of limitations against the employer for six (6) years under § 6502(a)(1), the government must assess the tax and give notice to the taxpayer-employer pursuant to § 6303(a) within sixty (60) days of the assessment. It makes no sense that Congress, in creating the derivative liability of a lender, would allow extension of the statute of limitations against the lender without notice of the assessment.

Under the government's view, the lender would not be apprised of non-payment or assessment, would not be given notice of assessment and would not know that he may be claimed to be derivatively liable for said assessed taxes under Treas. Regs. § 31.3505-1(d)(1), engrafting § 6502(a)(1) and extending the period for collection for six (6) years after assessment of the employer. Since the liability of the lender is derivative of the liability of the employer, surely the procedural safeguards afforded the employer must at least be afforded the lender, particularly since such safeguards were not specifically withheld by Congress.[8]

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[8]The government lamely argues that it is simply impossible to give lenders notice of assessment because its administrative practice does not provide for a quick determination of who the lenders are and that such a procedure would place such an

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### 3. The Third and Ninth Circuits Erred in Statutory Construction of the Interplay Between § 3505 and § 6303(a).

The Third and Ninth Circuits in *Jersey Shore* and *Hunter Engineers,* respectively, ignored the canon of construction set forth by this Court in *GTE Sylvania, supra.* Only by strained effort could it contort the unambiguous phrase of § 6303(a) "each person liable for the unpaid tax" into the phrase "taxpayer so assessed," and thereby render null to the lender the procedural safeguard afforded the employer.

Those courts reviewed the Reorganization Plans for the Internal Revenue Service promulgated by President Truman in 1950 and 1952, the resulting consolidation of functions in the Secretary and abolishment of the office of Tax Collector, to find what each court considered a "clearly expressed legislative intention" that notice was dependent on the means of collection rather than the per-

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onerous burden on the government that § 3505 liability would be an effective nullity. Such an argument bemoans a certain bureaucratic malaise. For example, the government could reform the employer's tax return under § 6011(a) to list all lenders and give them notice after assessment; make a supplemental assessment under § 6204 if the first is incorrect "in any way", and then give notice; or simply delay assessment until after investigation of the non-payment of taxes has been completed within the time frame of § 6501(a). In any event, this lame argument has no application to the situation where the government has actual knowledge of the lenders identity before assessment and/or notice. *See United States v. Merchants National Bank of Mobile,* 772 F.2d 1522 (11th Cir. 1985), petition for *cert.* pending, No. 85-1480.



son (being the Secretary) who commences the collection process. Their collective reasoning was in error.

First, § 6303(a) does not refer to the means by which collection activities are commenced by the Secretary. It purely, simply and directly requires the Secretary to give notice after assessment. All means of collection are vested in the Secretary. Thus, the clear language of § 6303(a) applies to the person initiating collection activities, and not the means by which collection is accomplished. Had Congress intended such a distinction after having merged the functions of collection and abolished the two separate offices responsible for collection, it could have easily said so.

Second, prior to adoption of § 3505 in 1966, the § 6303 (a) notice to the employer given by the Secretary after assessment was required whether the Secretary intended to collect the taxes from the taxpayer-employer by administrative means or by later civil action pursuant to § 7401.[9] The notice is therefore not dependent on the means chosen, but is binding on the Secretary as the officer charged with collection of taxes after assessment, whether by administrative means or litigation.

Finally, the Third and Ninth Circuits focused on the legislative history of § 6303(a), and ignored entirely the legislative history of § 3505. The general notice rule of § 6303(a) preceded adoption of § 3505, and applies as a

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[9]While the failure to give such notice would not bar the Secretary from bringing suit against the taxpayer with the statutory duty to pay the tax within the normal limitations period, *supra,* note 3, it should prevent extension of the statute of limitations based on such assessment.

general rule "unless otherwise provided." Section 3505 does not "otherwise provide" and there is nothing in its legislative history to indicate that Congress intended to provide otherwise, as noted by Judge Weis in his dissent in *Jersey Shore*. 781 F.2d at 984.

The Third and Ninth Circuits erroneously adopted the administrative practice of the government as its guide through the statutory framework for collection of § 3505 liability, rather than apply the statutes to govern such practice.

There is no clearly expressed legislative intention that the words employed by Congress in § 6303(a) should not receive their plain meaning. *Quinlivan v. Commissioner*, 599 F.2d 269 (8th Cir. 1979); *cert.* denied 444 U.S. 996, 100 S. Ct. 531, 62 L. Ed. 2d 426 (1979); *Conway County Farmers Association v. United States*, 588 F.2d 592 (6th Cir. 1978). The government asserts that a § 3505 lender is a person liable for the unpaid tax, so it must be bound by the everyday, ordinary sense of those words as Congress used them in § 6303(a).

### B. Failure to Give the Lender § 6303(a) Notice Bars § 3505 Liability.

The Seventh and Eleventh Circuits in *Associates* and *Merchants National Bank of Mobile*, respectively, held that the consequences of the failure of the government to give the lender § 6303(a) notice was an absolute bar of § 3505 liability. The government counters these holdings by arguing herein, as it did in the Eleventh Circuit, that it is not required to give notice of an assessment because any action against the lender is merely a common law action on a debt.



The common law action on a debt as argued by the government refers to actions against a taxpayer who bears a statutory duty to pay a tax. That rationale simply does not apply in a § 3505 action,[10] for the lender is liable only under certain limited circumstances and has no duty to pay the tax, only a duty to pay a judgment imposing civil liability under § 3505.

The Seventh Circuit in *Associates* noted that there was a fundamental reason for a lender to receive notice, stating:

> Section 6303(a) requires notice of the assessment of unpaid taxes in order to protect the taxpayer, *Macatee, Inc. v. United States*, 214 F.2d 717, 719 (5th Cir. 1954), and this rationale applies regardless of which collection mechanism is used.

721 F.2d at 1100.

Thus, once the government proceeds with the assessment of the tax, it must adhere to the statutory requirements of § 6303(a) notice to a lender, so as not to leave the lender at the mercy of the government for collection of § 3505 liability. There are important policy considerations in requiring the government to give § 6303(a) notice to extend the statute of limitation under § 6502(a)(1). Judge Weis, in his dissent in *Jersey Shore*, adequately pointed these out:

> The net affect of the Code revision urged by the IRS is to give less procedural protection to one secondarily liable than to the primary obligor. The notice of

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[10]Section 3505 liability is not and has never been a common law debt of a taxpayer. Rather, it is a derivative liability of a third party under limited circumstances created by statute, and enforceable, if at all, pursuant to the enforcement statutes of Subtitle F. *United States v. Merchants National Bank of Mobile*, 772 F.2d 1522, 1524, n. 1 (11th Cir. 1985).

> assessment will alert the taxpayer directly liable to the lengthened statute of limitations. He may then preserve pertinent records, arrange for payment, compromise, or take other steps in his own best interests. Without notice of the assessment, however, the party under § 3505 may not be alerted to his continuing exposure and concomitant risk. I am not convinced that Congress intended such an anomalous result.

781 F.2d at 984.

Since the lender stands unprotected without notice, the failure of the government to give same must constitute a bar to a civil proceeding to collect § 3505 liability from that lender.

**III. The Government May Not Validly Extend the Statute of Limitation to Collect § 3505 Liability.**

**A. The Framework for Extension of the Limitation Period.**

The statute of limitations on assessment and collection of unpaid taxes is set forth in § 6501(a), which provides as a general rule, the following:

> Except as otherwise provided in this section, the amount of any tax imposed by this title shall be assessed within 3 years after the return was filed (whether or not such return was filed on or after the date prescribed) or, if the tax is payable by stamp, at any time after such tax became due and before the expiration of 3 years after the date on which any part of such tax was paid, *and no proceeding in court without assessment for the collection of such tax shall be begun after the expiration of such period.* [Emphasis added].

This general three (3) year statute of limitations predates the adoption of § 3505 in 1966. Congress provided no specific statute of limitations for § 3505 liability, and hence,



the general rule of § 6501(a) applies, particularly since Congress did not authorize the government to separately assess the § 3505 tax liability.

Section 6502(a)(1) operates as an exception to the general rule as to collection of unpaid taxes *after assessment*, and provides:

> Where the assessment of any tax imposed by this title has been made within the period of limitation properly applicable thereto, such tax may be collected by levy *or by a proceeding in court*, but only if the levy is made or the proceeding begun—
>
> (1) within six (6) years after the assessment of the tax . . . . [Emphasis added].

In adopting § 3505, Congress did not provide for any specific extension of the statute of limitations for § 3505 liability. However, the government has engrafted §6502(a)(1) into the Treasury Regulations promulgated under § 3505, providing at Treas. Reg. § 31.3505-1(d)(1) as follows:

> In the event the lender, surety, or other person does not satisfy the liability imposed by section 3505, the United States may collect the liability by appropriate civil proceeding commenced within six (6) years after assessment of the tax against the employer.

**B. The Government May Not Extend the Statute of Limitation for § 3505 Liability Since There is no Separate Assessment.**

In enacting § 3505, Congress did not give the government the authority to assess § 3505 liability, *United States v. First National Bank of Circle*, 652 F.2d 882 (9th Cir. 1981); *United States v. Dixieline Financial, Inc.*, 594 F.2d 1311 (9th Cir. 1979), and did not set forth any statute of

limitation for same or guidelines for any alleged extension of said statute of limitation for § 3505 liability after assessment of the employer. The government took it upon itself to provide in the Treasury Regulations that it may arbitrarily extend the statute of limitation after assessment against the employer, engrafting the provisions of § 6502 (a)(1) into the procedure and administration for collecting § 3505 tax liability, even though Congress did not specifically give it that power.

Section 6502(a)(1) begins with the phrase "[w]here the assessment of any tax imposed by this title has been made . . . ". An assessment of tax is made under § 6203 "by recording the liability of the taxpayer in the office of the Secretary . . . ".

The liability of a lender under § 3505 is not assessed nor recorded in the office of the Secretary.[11] Since any assessment was made against the taxpayer-employer by recording the liability of the taxpayer-employer in the office of the Secretary, then it would appear clear that such assessment, relating only to the employer's statutory duty to pay said taxes, cannot apply to an unassessed leader for § 3505 liability.

Therefore, there being no exception by assessment of the lender to the § 6501(a) general three (3) year statute of limitations provided by Congress, that § 6501(a) statute of limitations is always binding on the government in § 3505 actions.

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[11]Arguably, § 3505 liability is not a "tax imposed by [title 26]" since § 3505 merely defines those circumstances in which liability attaches rather than creates a statutory duty to pay the employment taxes.



Any purported extension of this statute of limitation by a Treasury Regulation engrafting § 6502(a)(1) into proceedings for collection of § 3505 liability is clearly unauthorized, as there is no Congressional mandate that directs or provides for such an extension. For lack of such a mandate, the regulation is invalid. *Rowan Companies, Inc. v. United States*, 452 U.S. 247, 101 S. Ct. 2288, 68 L. Ed. 2d 814 (1981); *Chen Chi Wang v. United States*, 757 F.2d 1000 (9th Cir. 1985); *First Charter Financial Corp. v. United States*, 669 F.2d 1342 (9th Cir. 1982).

### C. At a Minimum, Failure to Give § 6303(a) Notice to a Lender Prevents Extension of the Statute of Limitation.

Even if the government may validly engraft § 6502(a)(1) into the Treasury Regulations under § 3505 to extend the statute of limitation, the failure of the government to give § 6303(a) notice to the lender of the assessment of taxes unpaid by the employer must be a bar to extension of the statute of limitation as to the lender.

The government has consistently argued in each of the appeals in the Seventh, Eleventh, Third and Ninth Circuits, respectively, that for purposes of § 6303(a), the assessment applies only to the administrative collection process. As the argument continues, notice of assessment is therefore only required to be given by the government to those persons subject to administrative collection proceedings, in other words, the taxpayer-employer, and not to a lender derivatively liable for said unpaid taxes under § 3505.

Yet, the government also assert that the act of assessment, which allegedly relates only to the administra-

tive collection process, also applies to "appropriate civil proceedings" under § 7401 to collect § 3505 liability, by extending the statute of limitation against a lender through the Treasury Regulations which engraft § 6502(a)(1).

These two positions are logical contradictions.[12] Either assessment does not apply to or effect § 3505 liability, such that no § 6303(a) notice is required and no extension of the statute of limitation after assessment of the employer is allowed, or assessment does apply to the government's procedure for collecting § 3505 derivative liability by appropriate civil proceeding, such that § 6303(a) notice is required and the statute of limitation for collection of said liability may be extended under the Treasury Regulations which engraft § 6502(a)(1).

There are also important policy considerations in giving notice as a prerequisite to extending the statute of limitation against a lender. For example, corporate officers of the taxpayer-employer may attempt to pass liability for the taxes to a lender under § 3505 to avoid potential liability under § 6672 for responsible officer penalties. Their interests are diametrically opposed to that of the lender. It would be unjust and prejudicial for the employer and corporate officers to have notice of assessment so that defenses to such penalty can be prepared, while the

[12]Both § 6303(a) and § 6502(a)(1) appear in Subtitle F of the 1954 Code. Both relate to the duties and responsibilities of the government after assessment of the tax unpaid by the taxpayer-employer. The government's illogical position is that a lender liable for § 3505 derivative liability does not qualify as "each person liable for the unpaid tax" under § 6303(a), but does qualify as a person liable for the tax and bound by the effect of the assessment against the employer under § 6502(a)(1). The government simply cannot have it both ways.



lender is given no notice to prepare a defense for potential §3505 liability. *See United States v. American Bank & Trust,* 623 F. Supp. 708 (E.D. Pa. 1985), appeal pending, No. 85-1615 (3rd Cir.).

Ordinary statutory construction dictates the conclusion that failure to give § 6303(a) notice to a lender alleged to be subject to § 3505 liability must operate to prevent extension of the statute of limitation. Otherwise, the government can merely choose which provisions of Subtitle F it wishes to abide by and which others it chooses to ignore.

## CONCLUSION

For the foregoing reasons, the judgment of the Third Circuit Court of Appeals should be reversed.

Respectfully submitted,

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August, 1986

## APPENDIX

U.S. Department of Justice
Office of the Solicitor General
Washington, D.C. 20530

July 14, 1986

Alan C. Christian, Esq.
Johnstone, Adams, Howard, Bailey
and Gordon
104 St. Francis Street
Eighth Floor
Post Office Box 1988
Mobile, Alabama 36633

Re: Jersey Shore State Bank v. United States of America, No. 85-1736

Dear Mr. Christian:

As requested in your letter of July 9, 1986, I hereby consent to the filing of a brief amicus curiae on behalf of Merchants National Bank of Mobile in the above case.

Sincerely,

/s/ Charles Fried
Solicitor General

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July 21, 1986

Alan C. Christian, Esq.
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P.O. Box 1988
Mobile, Alabama 36633

Re: Jersey Shore State Bank v. United States
No. 85-1736
United States Supreme Court

Dear Mr. Christian:

Pursuant to Rule 36 of the Rule of the United States Supreme Court, Jersey Shore State Bank, as Petitioner in the above captioned matter, hereby gives its consent to the filing of an amicus curiae brief by Merchants National Bank of Mobile on behalf of the said Petitioner.

Very truly yours,

CARPENTER, HARRIS
& FLAYHART

/s/ Martin A. Flayhart

cc: Hon. Charles Fried
Solicitor General